THE NATIONAL CITY BANK OF NEW YORK

1932

Economic Conditions
Governmental Finance
United States Securities

New York, October, 1932

General Business Conditions

THE past month has brought further evidence of emergence from the period of panic and credit strain, and likewise indications of the expansion of business activity for which everyone has been so anxiously watching. The improvement has proceeded unevenly, and its failure to reach the heavy industries with more vigor has been viewed in some quarters as a cause for disappointment. Where this is the feeling, however, the fault is in too high expectations. Experienced observers understand that the first impetus for the upward move comes from the exhaustion of stocks of apparel and other goods of every day necessity, which are used up faster than they are replaced, leading inevitably to a renewal of buying and of production to take care of current needs. The pickup now taking place is largely of this character. The improvement in industries whose products are less urgently needed awaits gains in purchasing power, the carrying out of replacement and expansion projects, and the growth of confidence promoting capital investment. Therefore it comes more slowly.

The financial improvement has continued. Currency is coming back from hoarding and gold is coming to this country from abroad. Together they are replacing Federal Reserve Bank credit in the banking reserves, and this is a desirable change, for Reserve Bank policies have been subject to a good deal of misinterpretation and a cause of misgiving in some places, whereas everyone understands that additions to the credit base through return of currency and gold receipts are wholly favorable. Thus the change is not only helpful to the banking position, but promotes the confidence that is necessary if the credit is to be used.

Security and commodity prices have given evidence of some tempering of the enthusiasm developed during August. Probably the uncertainties always connected with a national election cause hesitation, though neither party has endorsed policies giving occasion for alarm, and indeed their differences are minor. However, it may be doubted that the campaign is the major factor. There are abundant reasons, without considering politics, for maintaining a temperate view of the improvement, and most of them may be summed up in one reason, namely, the continued inability to do business on profitable terms. It must be considered that there is no probability of an increase in productive activity that will put any substantial proportion of the unemployed back to work this Winter, nor of such a rise in the prices of farm products as would restore the lost buying power of the farmer. It is a truism that prosperity will not be regained until the purchasing power of the population is restored, and if all the elements in the problem of restoring purchasing power are considered there is little basis for expecting a sensational or overnight recovery.

The foregoing is not written in any spirit of pessimism. Rather we consider it fortunate that business men are not assuming that a return to pre-depression conditions is just around the corner. Undoubtedly it is to the general interest that any tendency toward excess of optimism should be restrained. Not only may the disappointment following extravagant expectations bring a renewal of pessimism and distrust, but there is danger that the recovery may be thwarted if a too confident belief that the road is clear be allowed to weaken the attack upon the remaining problems of adjustment.

The Improvement in Textiles

This Letter last month referred to the showing of the textile industries during August as a "very vigorous recovery," and the figures now at hand reveal that this description was a moderate one. The paralysis of business in the Spring months had reduced textile production to the lowest level of modern times and, of course, well under consumption; and when the Government informed the trade in August that the cotton crop was shorter than expected the rush to cover requirements exceeded any previously known even in boom times. Sales of staple cotton goods reported by the Associa-

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tion of Cotton Textile Merchants reached the record total of 510,000,000 yards, nearly three times production. Of course this buying covered early needs, and September has been a quiet month, with cotton prices reacting very sharply. But the mills at the beginning of the month had net unfilled orders equal to six weeks' production at the August rate, and an increase in mill operations has occurred which is giving more employment, consuming more raw materials, and thus giving more support to business in other lines.

Cotton mills are large users of rayon, and for the rayon manufacturers likewise sales during August were larger than in any other month on record. Moreover, they have been unable to meet the demand for prompt deliveries, and forward buying has continued during September on such a scale that the month's sales may prove equal to August.

The woolen and silk industries also have had a very satisfying spurt, and September as well as August has been a good month. It is estimated that one-third of the domestic clip of wool was sold during August, and the trend of prices since has continued upward with cloth markets active and advancing. Mill takings of raw silk in August were larger than in any previous month on record with one exception, and have been heavy in September also.

This upswing in the textile lines is evidence of the great demand for merchandise that must be satisfied in this country, even in depression, whenever a period of under-buying has reduced consumers' and merchants' supplies to a minimum. Of course it is necessary for the merchants who have bought the goods to pass them on across their counters, but there are encouraging reports as to retail trade also. Beginning after Labor Day, an increase in sales took place which, according to preliminary estimates, has been of normal seasonal percentage, and this is a gratifying contrast with last year, when the seasonal increases were not realized.

The First Turn in the Indexes

There are gains also in other industries. Shoe business has picked up, with prices higher, and the hat makers are very busy. The late Summer expansion in coal production was sharper than usual, and lumber sales have had a good spurt, running substantially above production for a number of weeks and accomplishing much needed statistical improvement. With the textiles these gains were sufficient to turn some of the composite indexes of business, adjusted for seasonal influences, upward in August for the first time in a year or more; and for September representative weekly figures such as car loadings and consumption of electricity show a further advance, though it is scarcely necessary to say that the figures are substantially lower than one year ago, and still close to the lowest of the depression.

Little support has been derived from the important steel, construction, and automobile industries. Steel mill operations at the low were at 13 per cent of capacity, and the latest figure was 17½ per cent. Awards of building contracts continue to give evidence that the industry is on bottom; up to the 22nd of the month the daily average figures were even with August, but 50.5 per cent below one year ago. Automobile sales give some encouragement, having shown rather better than seasonal improvement, but the totals are extremely low and production in most plants is curtailed in preparation for the introduction of new models toward the end of the year. From these preparations the steel industry takes hope for a fourth quarter pickup.

Policies of the Government

If the efforts made by the Federal government and upon its initiative to promote business recovery have played a part in the current improvement, obviously the influence has been only an indirect one, exerted through support of the credit situation. This is wholly a cause for satisfaction. It is proof that business has within itself a capacity to recover, through the operation of supply and demand in working out adjustments in the markets, and under the stimulus of the wants which, after the paralysis is overcome, everyone seeks to satisfy as far as means permit. During the long period of panic and irresistible deflationary influences it was easy to lose sight of this natural recuperative power, and it is heartening to have a demonstration of it again.

It is agreed by nearly all economists and business leaders that the support given by the government to the existing economic organization has been vitally necessary, and instrumental above all other factors in neutralizing the effects of panic. The support was centered at the point where the organization proved most vulnerable to the influences of fear and depression, namely, the credit system and the credit-granting institutions. It was essential to maintain them if the economic organization was to be maintained, and it was essential to maintain the organization in order to bring recovery. Individuals were no longer able to maintain it because the instinct of self-protection is strong in individuals, and they yield to it and give way to panic more readily than they cooperate at their own risk for the common good. In the extremity leadership devolved upon the government, and it has been assumed in the manner familiar to all.

For the extension of the governmental functions beyond the point of supporting the economic system, such as has been provided in

the authorization of Reconstruction Finance Corporation loans for projects ordinarily dependent upon private capital and credit for their financing, endorsement must be more reserved; and any further proposals which may be urged upon the next Congress for the use of the national credit should be unreservedly opposed. Plainly there is a limit to the quantity of public credit that can be created safely. The country would be blind to the lessons of the past year not to bear in mind that alarm concerning the safety of the dollar was the most powerful of all the causes of deflation and panic, and that dissipation of the alarm was synonymous with termination of the panic.

Evidently it should be also considered that extension of government activities may give rise to an unsound optimism, resting on the assumption that the government has taken charge of conducting the nation back to prosperity. The danger is in leading individuals to the conclusion that they may leave the task to Washington and devote themselves to speculative anticipation of better times. If such a view exists, it is no reason for confidence. The business of this country is overwhelmingly in the hands of individuals, and consists of a vast and complex exchange of goods and services between them and the construction of facilities for producing the goods and services, in which the government normally and properly plays but small part. When this business falls off it is quite out of the question for the government to carry on sufficient added business of its own to fill the gap. All the expenditures the government can make cannot compensate for the loss of purchasing power on the farms and in the industries, nor can the employment it gives make up any important share of the employment that is lost through the decline of self-supporting industry.

Moreover, government expenditures cannot indefinitely continue in the face of a decline in self-supporting industry, for there must be production and profits to enable the people of the country to pay taxes and to subscribe to government loans. Finally, government expenditures of any kind can do nothing to correct the causes of depression; they will aid industry while they last, but industry will not continue unless it pays, and when the government comes to the end of its resources the situation will be the same unless adjustments have been made that will enable business to be done on profitable terms.

Unquestionably government intervention in business in normal times is a disturbing influence. The principle should be kept in view, since it will be necessary to come back to it, that a healthy business needs no government aid. It is important that business should render itself independent of the government as soon as possible.

Reduced Demands on the R. F. C.

These are the principles which in the general interest should control the policies of government at this stage of the depression. Fortunately demands upon the Reconstruction Finance Corporation are diminishing, with the subsidence of the panic and of demands on the banks. The advance in bonds has increased the assets of the banks and the advance in commodities has improved their loans. The demand for policy loans from insurance companies has also declined. Repayments to the Corporation are in good volume, and the allotment of Treasury funds to it, which in June was $245,000,000, in July $150,000,000, and in August $115,000,000, was in September, up to the 23rd, only $14,000,000.

Beyond doubt the greatest service that government, both Federal and local, can render in the present situation is to enforce economies that will balance their budgets and preserve their credit without resort to further taxation, and will permit tax relief at the earliest possible date. In truth the burden of taxation, greater than was borne when the national income was around ninety billions of dollars annually, is more than doubled when it must be paid out of an income diminished by more than half.

Finally it may be said that business in the coming months will need, more than government funds, the cooperation of all governments to aid the liberation of world trade from the restrictions that are throttling it, and in adjustment of the war debts in a manner to promote confidence and remove an unsettling and deflationary influence. The Stresa conference upon Danubian questions in the past month has furnished another encouraging illustration that under the spur of their necessities the nations are gaining in ability to cooperate. This conference arranged a plan, subject to ratification, for the creation of a fund by contributions of the adhering States, out of which will be paid premiums upon the export of grains from the Danubian countries. These countries for their part obligate themselves to give or continue trade concessions to the contributing States. This is a heartening recognition that cooperative measures to restore the flow of trade are needed. Even though the accomplishments of the conference fall short of hopes they contrast favorably with all previous attempts to deal with these difficult questions, which have yielded no results, or even caused fresh trouble.

Farm Prices and Purchasing Power

Commodity markets moved less in concert after the first part of September, and reactions

in the prices of some of the important farm staples have given warning against overdrawing hopes of relief from that quarter. Wool, eggs and butter have advanced further, and wheat, cattle and lambs held their ground, but hogs are lower on the month and cotton has had a severe reaction. The cotton advance in August had been sensational, and when on September 8th the Crop Reporting Board estimated the yield at 11,310,000 bales, instead of well below 11,000,000 as had been expected, the market was not in position to meet the shock, and the speculative support needed to absorb the hedge selling faded away.

The decline has attracted the attention of the Texas Legislature, which has memorialized Congress "to prevent a recurrence of the unwholesome demoralization and malicious destruction of values" that allegedly followed the crop report. The legislators have chosen an inappropriate time to pass resolutions against speculation, for the rise since June impressively illustrates the speculators' services in the markets. There is no shortage of cotton or other farm products and little increase in their consumption, but prices advanced sharply because informed people saw hope of improvement and were willing to risk their capital upon it, and therefore brought about the price advance long before it could otherwise have occurred. The farmer is the beneficiary. Speculators in the cotton market changed their price views when they found that an element in their calculations had been wrong; but this year as always the support of speculative purchases, without which the farmers' selling during the crop moving season would demoralize the market, is needed. The cotton market is but working out the price level upon which buyers will be found to carry the stocks.

This stop in the advance of farm prices adds weight to the warning uttered in this Letter a month ago, when it was stated that a rise in raw material prices sufficient to close the gap between what the farmer sells and what he buys was not anticipated, and that "it will be necessary to keep on closing it through reduction of costs if recovery is not to be gravely delayed." The farmer is no longer losing ground in price relationships as he did prior to June or July of this year, when the prices of his products were declining faster than those of the things he bought, but his gains have been small, and as long as he can obtain for his production but little more than half the quantity of other goods that he could before 1914, the basis for business recovery is unsatisfactory. The lack of balance between wages, transportation costs and many other costs on the one hand, and farm prices on the other, is the most serious maladjustment in the business situation. Moreover, the farmer is not the only or even the chief sufferer, in view of the fact that he can raise his own living. The lot of the factory worker thrown out of employment, because the farmer cannot buy the product of his labor, is worse.

The Wage Question

The wage question is the crux of the situation thus described, and it is a difficult question to deal with, because opinions upon it are strongly held and feeling is easily aroused. It is, however, a complex subject upon which opinions may honestly differ, and as it is one of great importance, all sides should be considered fairly and carefully, with the purpose of arriving at the truth of the conflicting views.

A proposal to reduce wages naturally meets with disfavor, not only among the wage earners whose pay is in question but with the public. Everybody prefers to hear of wage increases, which are usually understood as increasing the purchasing power of the recipients and as signs of prosperity. It is assumed offhand that if all wage workers could have their pay increased they would be able to buy more of the things that would add to their comfort and happiness, and that this would increase the demand for such goods, thus creating more employment, supporting the industrial system upon a higher level of compensation, and providing a higher standard of living for all. Per contra, it is assumed that if money wages are reduced purchasing power will be reduced, less goods will be made and consumed, and both employment and the standard of living will be affected. Of course, nobody wants such a shrinkage of purchasing power or lessening of consumption. Every business interest would be injured by such a trend.

If the foregoing assumptions were true there would be no industrial problem, but several fallacies may be pointed out. Insufficient account is taken of the relation between wages and the prices which consumers must pay for industrial products. Even when this relation is considered it is often assumed that, since wages are only a part of production costs, increased wage rates will give more purchasing power to the worker through the pay envelope than they will take from him in the increased price of the product when he comes to buy it. But this is clearly fallacious because the gain in purchasing power will be at the expense of all others who must pay the higher prices for the product, and as they reduce their purchases fewer goods will be made and less employment offered to the workers.

It is the rule of business that an employer's costs are passed on to the consumers of his product, which obviously reduces their pur-

chasing power to the same extent. The rise of living costs which accompanied the rise of wages during the war is familiar and is discussed elsewhere in this issue (page 158). In like manner, wage reductions, by reducing production costs, lead to a reduction of prices and enlarge the ability of consumers to buy.

In the present situation living costs are being sustained much above the pre-war level by the existing wage rates. Although numerous wage-reductions have been made and have effected a substantial reduction in living costs, the reductions have not kept pace with the loss of cash income of consumers not receiving these wages. Consequently prices of goods bearing these wage costs have not been lowered as rapidly, the basis of exchange has been disrupted, and unemployment has followed with all its attendant distress, giving further momentum to the vicious circle of the decline in trade.

Another fallacy is the argument that the standard of living is impaired by wage reductions. The standard of living is determined by the "real" wage, and the real wage is the product of the money wage rate per day or hour multiplied by the number of days or hours worked, divided by the price of the things the worker must buy. If a lower money wage rate is offset by a larger number of hours worked, and by reduced prices of the things bought, there is no loss in the real wage and none in the standard of living. In truth the gains in living standards of American workers have not been achieved by way of the money wage rate, but through improvements in industrial organization and equipment which have made it possible for them to produce more, and therefore to buy at lower prices, or to receive a higher money wage without equivalent increase in prices.

The Origin of Buying Power

The stress which is laid upon the importance of money wages as buying power implies that money is itself an original source of purchasing power, which it is not. Money in the ordinary sense—currency—no more originates purchasing power than railroad cars originate traffic. Both are facilities of trade, but they do not create trade or supply the impulse to trade. Specialization in industry and diversity of production are the basis of trade; goods and services of different kinds pay for each other, and create demands for each other. The farmer's buying power is in the products which he sends to market. The workers who make shoes have their buying power in shoes and the purchasing power of every group of workers is in the goods or services which it offers on the market.

The argument for the "high wage theory," as it has come to be known in this country, is that high wages are necessary to enable consumers to purchase the mass output of the factories. If the argument is applied to real wages it cannot be contradicted, and no one would desire to do so, but if it is confined to money wages and construed to mean that the higher such wages the greater the prosperity its errors may be pointed out. If the wages of everyone could be doubled the cost of capital, of land or rent, and of transportation would likewise soon be doubled and the prices of everything would be doubled, and no one would gain. Such a general increase would be no more effective in raising the standard of living than the act of pulling on one's bootstraps would be effective in lifting oneself over a fence.

Moreover, the "high wage theory" does not even contemplate pulling on both bootstraps, but only on one of them. If the wages of all the hired workers in the industries were advanced they could consume but part of what they could produce, and the increased cost of production and higher prices made necessary by their wage rates would close their market to the farm group, which for the most part does not receive wages, but receives prices for its products determined by open bargaining in a world market.

What the Census Figures Show

It is sometimes argued that the country is predominantly industrial, and that the farmers can be carried along by highly paid factory workers, but there is an error of fact in this argument, which the Census figures giving the distribution of the gainfully employed among the different occupations will show. In the Annalist of August 12 was published an analysis of the occupational Census of 1930 by Walter R. Ingalls, an economist and statistician of high standing, whose figures will be used.

Mr. Ingalls shows that out of a total of 48,830,000 gainfully employed, there were 9,550,000 operatives and laborers employed for hire in the factories, or a total of 14,111,000 in the manufacturing and mechanical industries including proprietors and officials, the building and printing trades, and a variety of occupations outside the factories in which men generally work for themselves, such as blacksmiths, bakers, tailors, etc. In agriculture there were 10,472,000 persons employed, of whom only 2,733,000 were hired, and in the production of all raw materials, including farm products, minerals, lumber and fish, 11,706,000 workers were engaged. The remainder were in domestic and personal service, salesmen, clerks, transportation workers, merchants, executives and professional men, etc.

It will be observed that the factory workers and producers of raw materials constitute two

groups so closely of a size that they must be considered of approximately equal importance in the social and economic organization. Either is so large that it is impossible for others to prosper if it is not prospering. If the theory we are considering were put to the test the apparent or temporary gains of the wage earners would be at the expense of all whose return for their services depends upon conditions in an open market,—of all the farm group and the vast number directly or indirectly dependent upon the farm group for their living. Of course the outcome would be the complete destruction of the economic equilibrium, and therefore chaos. This is the direction in which the country has been drifting in the last three years.

In short, the figures show, and the present situation also shows, that the interests of no group are paramount over others, and that none can prosper at the expense of others. There must be a fair balance among all and the balance must be maintained by the cooperation of all the people, and by their willingness to conform to economic conditions. The only possible way to restore purchasing power is to restore the exchangeability of goods and services.

Money and Banking

The striking feature of the financial situation has been the way in which the panic trends have been halted, and general monetary and credit conditions steadily strengthened. The turn in the tide of currency hoarding, the reappearance of gold previously withdrawn from the banking system, the revival of confidence in the dollar with accompanying large inflow of gold from abroad, the rapid accumulation of bank reserves, and the rise of security prices are indicative of a great change in the situation over the past two months.

For the first time there has been a definite break in the sequence of disastrous events that swept over the world after the failure of the Kreditanstalt in Vienna in May, 1931.

As a result of the foregoing developments, the Federal Reserve Banks have been enabled to suspend the open market operations undertaken this Spring to support the credit structure in the face of panicky demands made upon it by domestic and foreign depositors. Purchasing of Government securities was stopped early in August, and the volume of Reserve Bank credit outstanding has shown the first reduction since the program of Government security buying was inaugurated in the Spring.

In short, the vicious circle of fear and deflation has commenced to reverse itself. It is too early to say how long this will continue to be the case, for the situation is still delicate, and the adoption of ill-advised policies by this country or an unfavorable turn of events abroad might easily reawaken apprehensions recently so active. Unquestionably, however, the outlook is more hopeful than it has been in a long time.

Evidence of the decided improvement that has taken place in the condition of the banks appears in the statistics of bank failures. During September the number of suspensions was the smallest since April and less than half the average for the first six months of the year. Equally significant was the announcement by the Reconstruction Finance Corporation that the betterment in credit conditions has caused an important decrease in the number of banks applying for emergency loans.

The Decline of Hoarding

The indications as to a subsidence of currency hoarding continue favorable, thanks to the operations of the Reconstruction Finance Corporation in checking bank failures, the improvement in bank portfolios wrought by the recovery in the commodities and securities markets, and the generally better sentiment among depositors.

Since the first of July the demand for currency has again fallen off,—slowly during July but more rapidly thereafter as the feeling of confidence has grown throughout the country. August, which usually shows an increase in currency outstanding, showed a decrease of something over $34,000,000. Similarly, the flow-back of currency in September after Labor Day has been larger than usual, so that instead of the usual Fall increase the volume of currency outstanding on September 28 was the lowest since June and approximately $170,000,000 below the June-July peak.

Indicative also of the passing of the panic psychology has been the reappearance of gold which had been withdrawn in fear from the banking system during the Fall and Spring. According to the Treasury circulation statement for the end of August, the amount of gold coin and bullion in circulation decreased $4,600,000 during the month, the first important decline shown for any month since January. At the same time gold certificates outstanding decreased by $24,700,000, making the net decrease of gold in circulation $29,300,000.

The table on the next page gives data from the Treasury circulation statement showing the change in gold and other types of circulation during the month of August and over the past year.

It will be seen from the figures that despite all the talk about the gold standard, the hoarding of money in the United States was primarily a manifestation of distrust of banks and not of the currency. Although the amount of gold coin and bullion in circulation at the end of August was about $86,000,000 greater than a year previous, this represented only a small

proportion of the increase of $640,000,000 in total circulation, which was more than covered by the expansion of Federal Reserve notes.

Money in Circulation August 31, 1932
(In Thousands of Dollars)

	Change Since July 31, 1932	Change Since Aug. 31, 1931
Gold Coin & Bullion	— 4,609	+ 86,468
Gold Certificates	—24,739	—319,965
Standard Silver Dollars	— 22	— 4,029
Silver Certificates	— 806	— 30,388
Treasury Notes 1890	— 1	— 17
Subs. Silver	+ 974	— 15,872
Minor Coin	+ 173	— 3,848
U. S. Notes	— 3,902	— 15,695
Federal Reserve Notes	—45,046	+845,886
Federal Reserve Bank Notes	— 26	— 203
National Bank Notes	+43,793	+ 97,690
Total	—34,211	+640.027

Influence of New National Bank Notes

The figures in the foregoing table give confirmation to the view that the issuance of new national bank notes would not increase the total currency outstanding, the new bank notes simply displacing other forms of currency. Whereas national bank notes outstanding rose by approximately $44,000,000, this rise was almost precisely offset by the decrease in Federal Reserve notes outstanding which, together with the redeposit of gold and gold certificates, accounted for the reduction in the total circulation noted in the table.

We invite to the above figures the attention of all those who contend that the country is suffering from a shortage of currency which must be corrected by large issues of new notes before business can recover. The notion that business is limited by a scarcity of currency is a common error which ignores both the fact that the Federal Reserve Banks already have the power to issue all the currency the country needs and the fact that only a small part of the business of the country is carried on with currency anyhow, most transactions being settled by means of checks drawn against bank deposits.

Because everyone familiar with the situation has known that the available supplies of currency were adequate, and that new issues of currency would simply displace other issues without raising the total, the new currency law has not been regarded as an immediately dangerous measure. Nevertheless, it would be a mistake not to recognize the possibilities of danger in the future.

Up to the point where the facilities for obtaining new national bank notes have aided hard-pressed banks in reducing their indebtedness, thus easing the pressure for liquidation, they have served a good purpose. The danger lies in the possibility that the banks at some later date may avail themselves of the issue privilege on a large scale and that this, coinciding with the return of a billion or more of currency from hoarding, and gold imports, may have the effect of impairing the ability of the Federal Reserve Banks to control the market.

It is true that under present conditions of easy money and excess reserves, there is little incentive for the large city banks to avail themselves extensively of the new currency privileges. However, as soon as there is an increase in the demand for money sufficient to absorb the surplus funds now on the market, an increased issue of national bank notes by the large institutions might readily take place.

Gold Imports and World Gold Stocks

The monetary gold stocks of the United States continued to increase during September and by the 28th had reached a total of $4,185,000,000, a gain of $276,000,000 from the June low point and a level approximately equivalent to that in late 1928 and early 1929. The inflow is a reflection of reviving confidence in the dollar and of the strong creditor position of the United States in the international settlements. Signs of increased trade activity, coupled with a quieting down of alarm occasioned by the soldiers' bonus and other inflationary proposals in Congress last Spring, have stimulated a renewed foreign interest in our security markets. At the same time the large remittances which foreign countries have to make to the United States on account of merchandise trade and interest and principal due us on private debts, over a period when offsetting items in the form of new credits granted and American tourist expenditures are running low, have tended to swell the balance of payments in our favor, leading eventually to gold shipments.

Very little, however, of the increase of reserves of this country has been at the expense of the effective monetary stocks of other countries. Most of our gain has come from the release of funds earmarked at the Federal Reserve Banks for the account of European central banks, but without equivalent decreases in the gold holdings of the latter, since these banks have been able constantly to replenish their supplies out of gold coming into the London market from India, Africa and Australia. Of approximately $60,000,000 of gold physically imported into this country during this period, the greater part represented newly mined gold from Canada, the Philippine Islands and Australia, and gold that previously had not been included in monetary stocks, namely from India, China and Mexico. Japan was practically the only country from which we received gold out of existing monetary stocks.

The above facts are illustrated by the following table showing the recent changes in gold stocks of the United States and twenty-

one other principal countries. It will be seen that an increase of $270,000,000 in the gold stocks of the United States since the end of June was accompanied by an increase of $63,000,000 in the gold stocks of other countries during the same period. (In this table figures on gold stocks of the United States are given exclusive of gold in circulation.)

Gold Reserves of Central Banks & Governments
(Millions of Dollars)

	United States	21 Other Countries	Total 22 Principal Countries
End of Dec. 1931......	4,051	6,259	10,310
" " June 1932......	3,466	6,881	10,347
" " July 1932......	3,520	6,902	10,422
" " Aug. 1932......	3,638	6,913	10,551
" " Sept. 1932(est)	3,736	6,944	10,680
Increase June-Sept.	+270	+ 63	+333

An additional straw which is indicative of returning world confidence is the fact that gold coin shipped to Europe during the period of fright over currencies is now beginning to come back to this country. Since the United States is the only important country which pays out gold in small denominations, the demand for gold by small hoarders abroad concentrated on American gold coin, which was shipped abroad to the extent of something like $60,000,000 during the first half of the year. Now that the panic has subsided this gold is beginning to appear, and while the amount actually returned is still small, aggregating only about $3,500,000, the trend is significant. The amount of American gold coin absorbed by Europe represents only a portion of the substantial quantity of gold which disappeared in private holdings in Europe, and the reappearance of which would add substantially to monetary stocks throughout the world.

According to the latest available figures, the monetary stocks of 48 central banks and governments are now in the neighborhood of $11,500,000,000. Compared with August, 1928, this represents an increase of 16 per cent, a gain which effectively refutes any contention that gold shortage has been a factor in prolonging the depression. Of this increase, part has come from the enlarged output of the world's mines and part from the release of private holdings in India, China, Russia and Australia. During the current year it is expected that the new mining output will be close to the record total of $470,000,000 reached in the year 1915.

The Domestic Money Market

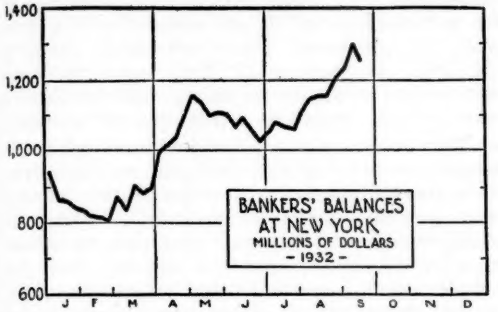
The foregoing movements with respect to gold, currency and national bank notes have developed a condition of extraordinary ease in the principal domestic money markets. The banks in the larger cities have been out of debt to the Reserve Banks for some time and with funds piling up, have been unable to find suitable investments, owing to the greatly reduced level of business and speculative activities. As a result, the volume of surplus reserves has risen to new high levels, in excess of $200,000,000 for New York City banks alone and over $350,000,000 for all banks in the weekly reporting system.

A natural outgrowth of the large volume of surplus funds now in the market and of continuing retirements of currency and inflow of gold would be a gradual reduction in the Reserve Bank holdings of Government securities. These holdings were purchased during last Fall and Spring for the purpose of putting Federal Reserve funds in the market at a time when the growth of currency hoarding and gold exports was causing a severe drain upon bank deposits. Now that the movement of currency and of gold has turned about and funds are flowing in upon the banks, a policy on the part of the Reserve Banks of permitting a portion of their shorter maturities of Governments to run off without replacement would be a logical development, and prevent the accumulation of idle funds from reaching excessive proportions. There is no reason to suppose that a decrease in the Reserve Banks' portfolio of Government securities, in step with the return of currency or gold, would be a disturbing element in the security market.

Money rates, in consequence of the pressure of idle funds, continue at minimum levels, Stock Exchange call money being pegged at 2 per cent; time money ruling at 1-1¼ for 60-90 day maturities, open market commercial paper at 2-2¼ per cent for best names, and 90-day bankers' acceptances at ¾ of 1 per cent. Yield rates on short-term Government securities range from 0.15 per cent to close to 3 per cent for maturities up to five years.

The condition of extreme ease represented as existing in the principal centers cannot be considered typical of the situation throughout the smaller cities and towns. There is no doubt but that banking conditions even in the smaller communities have improved considerably in recent months, but even so the situation in many localities is still tight. The monetary ease of the centers has been slow to percolate through the country. There is, on the contrary, a strong tendency for interior funds to gravitate to the centers, and particularly to New York. A reflection of this appears in the diagram on the next page showing a marked growth during the year of bankers' balances in this center, a trend which on first consideration seems somewhat surprising in view of the strained situation known to exist in the interior. Upon analysis of the figures, however, it will be seen that the increases have been due chiefly to increases in balances maintained here by banks in such larger centers

as Boston, Philadelphia, Pittsburgh and Chicago. There appears to be little tendency for such funds to get out into the smaller communities. Activities of the Reconstruction Finance Corporation have helped a great deal, and the facilities for obtaining new national



bank currency have also been useful. Nevertheless, there remains the anomaly of over $350,000,000 excess reserves in the banking system at a time when the volume of rediscounts is also at about that figure.

Such uneven distribution of funds is inevitable under our present banking system, composed as it is of thousands of separate units having no coordinated system of control or close connecting channels through which the idle funds of the city can be made available to the country.

An Upturn of Bank Credit

Accompanying the large increase of bank reserves, the downward curve of bank credit in use has given way to a pronounced upward trend. Thus far, however, there has been little evidence of an increased use of bank credit for business purposes. Loans and discounts of the weekly reporting banks continued to decline to new low levels for the year, notwithstanding the improvement noted in certain lines of trade and rise of security prices. The expansion of total credit in use has been in the bank holdings of investments, and especially of Government securities. During the four weeks ended September 21, which period included the Treasury's quarterly financing, bank holdings of Governments increased $490,000,000. This marks a new high record in bank holdings of Government obligations, by reporting member banks, such holdings now constituting 26 per cent of the total loans and investments.

Deposits of reporting banks on September 21 were up nearly a billion dollars from the July low point. This increase has been due to redeposits of currency and gold imports, but more particularly to book credits created by bank purchases of securities, principally Governments. During the week of September 21 Government deposits increased $456,000,000, reflecting subscriptions to Treasury issues on the 15th. The rise in total deposits over the past two months is the sharpest that has occurred since 1930.

The Bond Market

The market for high grade bonds continued strong during September although many of the more speculative issues, which had advanced rapidly during the two preceding months, reacted somewhat in sympathy with the stock market. Prime corporation, government and municipal bonds held steady, reflecting the prevailing low level of interest rates and the increase in excess reserves of the commercial banks resulting from gold imports and the return of hoarded currency. The passing of panic conditions which gripped the bond market in the early Summer and their replacement with confidence and a trend toward normal conditions are developments whose importance can hardly be overestimated.

An improvement is reported in the demand for bonds on the part of savings banks and insurance companies, which normally are very large purchasers of securities for investment. Deposits of a group of thirty savings banks in the second district, compiled by the Federal Reserve Bank of New York, have shown an upward trend for the past three months, following losses in May and June. In the case of the life insurance companies a decrease in the applications for policy loans has been noted in recent months, and figures reported to the New York Evening Post by twenty-nine large life insurance companies showed for the week ended September 21 the largest purchases of investment securities and mortgages since February.

New offerings made last month totaled approximately $103,000,000, the largest of which was $60,000,000 in one-year 4 per cent gold notes, callable after 9 months, of the Dominion of Canada at 100 and interest. The issue represents the first financing by the Canadian Government in the New York market this year and will be used in part to meet a 4 per cent issue of $40,000,000 maturing December 1. There was a considerable number of other new offerings but most of the issues were for relatively small amounts of municipals. The City of Boston sold $5,363,000 in serial 4¼s which were reoffered to the public on an interest basis to yield 2.25 to 4.10 per cent. Demand for industrial financing is naturally light, because the working capital of representative industrial companies is more than ample to handle the current volume of business, while the borrowings by municipalities are materially below normal due to the widespread movement for economy in public expenditures.

Rise in Municipal and Government Bonds

A feature of the municipal market last month was the rise of five points or more in the long-term bonds of the City of New York upon the change in administration and the announcement of renewed efforts to reduce expenditures with the purpose in view of cutting the budget between $75,000,000 to $100,000,000. All operating departments have been ordered to reduce expenditures by 20 per cent. Salaries of Mayor and Commissioners have been reduced voluntarily, and various alternative plans for further savings are under discussion. Representative issues such as the 4¼ per cent bonds due in 1981 are now quoted around 94-95, compared with a low price reached last June of 76-78 and a recent issue of corporate stock was sold on a 5¼ per cent basis, compared with a rate of 5¾ per cent previously paid.

In connection with the program of municipal economy, instituted in this and other cities, references are sometimes made to the "demands" of bankers as forcing salary cuts and other forms of retrenchment. Such statements are misleading, inasmuch as the conditions under which the market will absorb municipal securities are set not by the bankers but by the investing public. The position of the banker is solely that of a dealer who buys securities from the municipalities which he then distributes at a small margin of profit. The investor is the arbiter in these matters, but the banker naturally is expected to state to the borrower how much the market will take and on what terms.

United States Government financing during the month consisted of $451,447,000 in one-year Certificates of Indebtedness bearing 1¼ per cent interest and $834,401,500 in five-year Treasury Notes bearing 3¼ per cent, both dated September 15, together with $106,665,000 of three-months Treasury Bills dated September 28. Maturing issues during the month totaled $812,970,500. Subscriptions to the September 15 issues exceeded the allotments more than 6 to 1, while the Treasury Bills were also oversubscribed heavily and were awarded on an annual interest basis of 0.23 per cent, the lowest rate ever reached. Practically all of the United States Government bonds recently established new high prices for the year.

Railroad Wages, Taxes and Freight Rates

The action of the Class I railroads in requesting a conference with their employes upon the subject of a further reduction of wages, and the action of the brotherhood officials declining to entertain the proposal, brings the railroad situation to the front again, as a matter of pressing public importance. The situation was one of increasing gravity throughout last year on account of the declining revenues of the companies, the disastrous fall in the market value of their securities and the reaction of this loss of values upon the entire financial and business situation. The brotherhoods were sufficiently impressed by the indisputable facts to assent to a deduction of 10 per cent from the pay rolls for the term of one year from January 31, 1932, to January 31, 1933, upon the condition that at the end of this period the former rates of pay would be automatically restored.

This action was appreciated and acknowledged as showing an intelligent and cooperative attitude toward a problem which in fact was as much theirs as anybody's. The railroad situation is only part of a general situation in which not only this country but the whole world is involved and which therefore is not chargeable to either party of this controversy. There is a common problem to restore normal conditions in industry and trade, in which the railroad companies, their employes, all of the industries, all wage-workers, and indeed all people, are alike interested. During the excited, over-stimulated, inflated conditions which existed during the war and years following, which could not in reason have been supposed to be permanent, brotherhood wages had been increased until the average of hourly rates in the year 1931 was 157 per cent above the 1913 average. The brotherhoods' consent to a reduction of 10 per cent for one year was thankfully accepted as a helpful contribution to post-war readjustments, and the agreement was signed in the hope that with a general revival of business and increase of traffic it would be sufficient to enable the railroad industry to turn the corner.

Quite as much to the disappointment of the company officials as of the brotherhood officials, this hope has not been realized. In the first six months of 1932 the Class I railroads suffered a decline of 27 per cent in gross revenues and 53 per cent in net operating income in comparison with similar results in the corresponding period of last year, and a combined net loss of $127,384,000 after expenses, taxes and interest charges. Volume of traffic and earnings was affected by continuing decline in business activity, increasing unemployment and diminishing purchasing power throughout the country.

Although recent traffic returns indicate seasonal gains over preceding months, earnings are still so far below those of last year, and the outlook so uncertain, that the situation imperatively demands further constructive or remedial measures.

Lacking both earnings and the ability to refund maturing obligations, the problem of maintaining the solvency of the railroads has

become one calling for the most serious consideration on the part of all parties at interest, which includes practically everyone. Commercial and savings banks, insurance companies and other institutional investors own 70 per cent of the outstanding bonds and notes, the large body of employes whose livelihood comes from the railroads have a direct interest in the companies' welfare, and the very economic life of producers, merchants and the general public is dependent upon having adequate and economical transportation service.

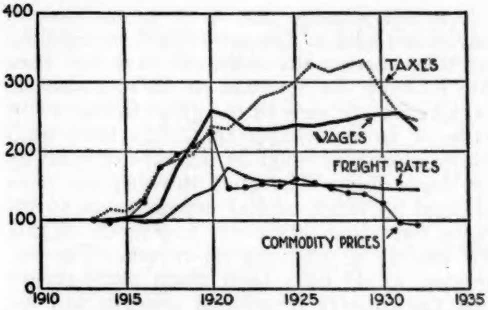
In order to meet the critical conditions the railroad companies have adopted drastic economies in operation and maintenance, the proceeds of the freight rate increase granted early in this year have been pooled with the Railroad Credit Corporation for loans to solvent companies not earning their fixed charges, Government credit has been loaned through the Reconstruction Finance Corporation to the aggregate amount of $319,000,000, and the companies have had the benefit of the 10 per cent wage reduction since February 1st. It is evident that the companies do not have the earnings or credit to finance themselves. They are in need of increased revenues or a reduction of operating costs, or both.

Freight Rates, Wages and Prices Compared

Any proposal for a general increase of freight rates at this time would be open to two serious objections, first, that rates already are high in relation to the value of commodities carried, and, second, that any increase in rates would cause a further diversion of traffic to motor trucks and other forms of competition.

That there should be regulation of competition is generally conceded, but when it will be had is something nobody knows. Moreover the country does not want a further increase in freight rates, particularly upon raw and bulky products, which are now so depressed in price. Transportation costs enter into the living costs of every family in the country, and their importance is increased by the fact that in many instances they enter repeatedly, as in the case of commodities that are shipped first as raw materials for fabrication, and later, perhaps more than once, as finished goods in distribution. Iron ore, coal and other materials used in making steel are shipped to the steel works, the steel is shipped for fabrication into automobiles, farm machinery or other saleable products, and shipped again to the localities where sold. The multiplied charges upon these shipments all enter into the prices which the ultimate buyer pays, and any increase in them lessens his ability to buy other things and therefore lessens the aggregate of possible employment. An increase of transportation costs would be a serious obstacle to business recovery.

The relation of freight rates to general prices, the growing burden of taxation and the rates of railroad wages, which make up approximately 65 per cent of railroad operating expenses, is shown by the accompanying diagram:



Index of Railroad Wages, Freight Rates, Railroad Taxes and General Prices Based on the 1913 Average

Note—The base represents averages for 1913. The index of wages is that of the National Industrial Conference Board prepared from the official reports of the Interstate Commerce Commission showing wages of all employes on Class I railroads and is based on the fiscal year ended June 30, 1915, the first year for which wages were reported on an hourly basis. This base is approximately the same as 1913, inasmuch as no important wage changes were made during the period 1913-1915. In June, 1932, hourly wages were 130 per cent above pre-war. Revenue per ton mile, also from the I. C. C. reports, is used for the index of freight rates, and for the first six months of 1932 was but 45 per cent above the 1913 average. The figures for taxes paid are also from the reports of the I. C. C. The wholesale price index is that of the Bureau of Labor for all commodities, which in July, 1932, had fallen to 8 per cent below the 1913 level, while the index of raw materials had fallen 20 per cent below 1913.

The maladjustment between freight rates, the railroads' principal source of income, and these principal regular expenditures is strikingly depicted by the chart. The line for general commodity prices is inserted to call attention to the burden imposed by the increase of operating costs upon the producers and consumers of commodities.

During the period of rising prices between 1913 and 1920, the price index rose about 126 per cent, railroad wages were increased by 159 per cent, but freight rates were increased by only 46 per cent, the disparity between the latter two largely accounting for the critical condition of railroad finances in 1920 when the roads were returned from government operation to their private owners. There had been general freight rate increases of 5 per cent in 1915, 15 per cent in 1917, 25 per cent in 1918 and 40 per cent in August 1920. This was followed by a 10 per cent reduction in 1922, which would have left a net advance of approximately 90 per cent, although the actual advance was much smaller on account of the constant whittling down of rates on specific commodities by the I. C. C. and, in many other

cases, by the railroads themselves in order to meet competition. New schedules for class rates, based largely on mileage, have been put into effect during recent years, while the emergency surcharges were put into effect January 4, 1932 to run until March 31, 1933.

It is not strange that with an increase of only 45 per cent in average freight receipts per ton mile carried the railroads have not been able to cover an increase of 157 per cent in wage rates. In view of the great falling off of traffic it is remarkable that they have been able to absorb as much of increase of costs as they have done. The good showing has been achieved by large capital expenditures to increase operating efficiency, and much of this new capital is receiving no return. The depression would have been much more severe upon the country if railroad charges had increased to correspond with the increase of wage rates.

The varying but general increase in freight rates may be illustrated from the following list of twelve important and representative agricultural products showing the rate per hundred pounds in carload lots between Chicago and New York in 1913 and at the present time (including sur-charge), with the percentage increases, together with the wholesale prices:

Freight Rates on Farm Products, Carload Lots, Chicago to New York and Comparative Prices in Chicago Wholesale Markets, 1913-1932

Commodity and Measure	Wholseale Prices Year 1913	July, 1932	Per Cent Change	Freight Rates Per 100 Pounds 1913	1932	Per Cent Change
Cattle ....cwt.	$8.507	$8.606	+1.2	$.28	$.53	+89
Hogs ....cwt.	8.365	4.856	—42	.30	.61	+103
Sheep ....cwt.	7.794	5.906	—24	.30	.665	+122
Wheat ....bu.	.986	.484	—51	.212	.38	+79
Corn ....bu.	.625	.319	—49	.212	.38	+79
Eggs ....doz.	.226	.133	—41	.65	.965	+48
Dressed Poultry lb.	.145	.156	+ 8	.50	.965	+93
Cheese ....lb.	.142	.112	—21	.50	.78	+56
Butter ....lb.	.310	.173	—44	.75	.965	+29
Meats (Beef) ....lb.	.130	.142	+ 9	.45	.81	+80

This table strikingly demonstrates the increasing burden of transportation charges caused by the increase of freight rates in the face of falling commodity prices.

Revenue per ton mile has shown a slight downward trend during the last few years, but the general price index has declined much more rapidly to a point 8 per cent below that of 1913, and a considerable number of individual commodities have declined to the lowest levels since the 1890s or earlier.

Effects of Increased Freight Rates Upon Business

Hardships arising from the increase of freight rates are illustrated by correspondence which we have seen between a lumber company in Philadelphia and two large railroads this Summer with respect to the difficulty of continuing in business with freight rates as high as at present. An extract from a letter written by the lumber company is given below:

On November 16, 1914, we shipped XYZ Car No. 182182, from our mill to McIlvain Siding, Phila., containing Birch and Maple lumber, freight	$ 85.15
If this car were shipped today, the increased freight on the same would be........	105.46
Total freight would be........	$190.61

I have gone over the records for shipment of lumber during 1914, and the value of the product of Appalachian Timber, delivered in Philadelphia, was approximately the same then as it is today. There would be very little difference.

We have just received and unloaded at our yard, a carload of hemlock dimensions, the freight on which was $169.36. Had the same carload of lumber been shipped over the same rails in 1914, the freight would have been $66.93. It is impossible for us or any other lumberman to be in the lumber business and furnish your rails with carloads under such nonsensical conditions.

This lumber company, which was incorporated more than twenty years ago as a subsidiary of an organization founded 134 years ago, recently announced that it had been forced to close down its plant entirely, and gave as explanation the unsatisfactory prices and volume at which its product was being marketed, the large increase in freight rates on lumber and the lack of encouragement that the railroads would in the immediate future be of any assistance in meeting the changed economic conditions.

Another case brought to our attention is that of a paper mill the owners of which, having under consideration an opportunity to shift from coal as fuel to crude oil, laid the conditions before the railroad company by which it was accustomed to receive coal. The reply expressed regret at inability to make a more favorable rate and said:

I am sure you are conversant with the conditions confronting the carriers at the present time and appreciate the seriousness of our situation, and if you should determine to change your fuel it would cause us to suffer a very severe loss in revenue right at a time when we can least afford it.

To which the paper company replied rather curtly as follows:

We are engaged in a business that must meet changed economic conditions or else close up. It is obvious that we cannot meet the changed conditions and deal with companies who refuse to meet changed conditions.

A large producer of coke recently informed us that whereas prior to the general price decline the total cost of distributing their product ranged from 45 to 50 per cent of its sales value, it now ranges from 75 to 80 per cent, and that various fuel substitutes are gaining a firmer foothold every day.

The above cases are typical of the difficulties that many manufacturing companies are having and their feeling that freight rates must be revised downward. Some of the trade associations representing manufacturers and deal-

ers in the lumber industry have recently started a movement for a reduction in freight rates to the approximate level of 1915 so as to correspond with the decline in commodity prices to the pre-war rate. Newspaper accounts of the meetings of leaders in the lumber industry state that:

They admit that the present depressed level of railway earnings must be taken into account, but the feeling prevails that operating costs can be cut sharply to permit rate reductions nevertheless. In particular, railway wages, taxes and prices of certain commodities such as steel rails can be brought down to permit a general rate reduction.

These instances are not given to support criticism of railroad managements but to illustrate the problems with which they have to deal and the problems of business men who are struggling to carry on. They are related to the unemployment situation. Many are confronted with demands for rate concessions which they cannot afford to grant, with the alternative of traffic losses even more serious.

Most of the complaints against railroad freight rates and indeed the whole industrial situation, are illustrated by the case of the anthracite coal industry, which is suffering from reduced consumption, said to be due in part to the sharp competition of other fuels, but undoubtedly is due in part to the impulse to economy given by the rise in price to consumers since the pre-war period. The anthracite operators have asked for a reduction of wages, which would affect about 140,000 miners, alleging that wage-rates are 174 per cent above the pre-war rates. The miners have refused to concede, asserting that the nominal rates do not signify much as to their earnings, on account of the reduced amount of employment. The operators and employers have joined in a petition for a reduction of $1 per ton in the freight rate on anthracite in order that retail prices may be reduced by this amount. The cost of such a reduction to the railroads would be about $50,000,000, which obviously they are not in a state to absorb. Will the railroad employes consent to absorb it in order to help the miners? Apparently not, for they allege that their own wages already are greatly reduced by short working hours. Meanwhile, however, the high cost of coal, in which miners' wage-rates and railroad wage-rates are the principal factor, is constantly diminishing the consumption of coal and the employment of miners and railroad employes.

The Burden of Taxation

Another outstanding feature in the railroad problem is the enormous tax bill of the railroads, which has been growing constantly until it has become an excessive and almost unbearable burden upon the companies, upon the cost of transportation and thus upon the price of all commodities. The expansion in tax assessments and the increasing share of revenues that goes for taxes may be seen from the following table covering selected years since 1900:

Railroad Taxes, In Thousands of Dollars, and Their Percentage to Earnings and Dividends

Fiscal or Calendar Year	Taxes Paid (000')	Percentage of Total Taxes Paid To: Gross Revenues	Net Rwy. Oper. Inc.	Dividends Paid
1900	$ 48,332	3.3	9.2	34.6
1910	98,035	3.5	12.2	27.9
1913	122,005	3.8	15.1	37.2
1920	289,272	4.6	*	105.1
1930	349,207	6.6	40.2	68.8
1931	307,707	7.3	57.8	93.5
1932 (6 mos.)	149,202	9.3	132.9	**

* No percentage calculated as net railway operating income declined to practically nothing.

** Not available.

Between 1900 and 1913, railroad taxes increased from approximately $48,000,000 to $122,000,000, or by 150 per cent, but earnings also increased and taxes in 1913 represented 3.8 per cent of gross revenues, 15.1 per cent of net railway operating income and 37.2 per cent of dividends paid. Between 1913 and 1931, however, taxes increased by another 150 per cent and were more than six times as large as in 1900. The levy of Federal, State and local taxes last year aggregated more than $307,000,000 and represented 7.3 per cent of gross revenues, 57.8 per cent of net operating income and was within 6.5 per cent of total dividend payments. For the first six months of 1932, more than 9 cents out of every dollar paid by the public to the railroads went for taxes and the tax collectors received 32 per cent more money than was available to the railroads themselves for meeting interest charges on their outstanding bonds. This condition shows the really desperate situation of the railroads at the present time and the urgent necessity that exists not only for the efforts at retrenchment which the managements are making, but for intelligent attention on the part of the public.

The chief responsibility for the increase of taxation does not lie with the Federal Government but with the taxing authorities of the various State, County, Municipal, and other political subdivisions. Of the total railroad taxes and assessments in 1930 (latest date available) amounting to $349,207,000, or $1,519 per mile, $40,986,000, or $178 per mile, went to the United States Government, whereas $308,221,000, or $1,341 per mile, went to States, Counties, Municipalities, etc. The railroads serving New Jersey, for instance, are taxed at a rate per mile 152 per cent higher than in any other State, equalling $9,951 in 1930 as compared with $6,255 in 1921—a gain in nine years of almost 60 per cent. This State,

furthermore, has been notably backward in adequate regulation of commercial motor trucks and buses.

There are several ways that railroads can attempt to reduce this enormous tax burden; not the least of which is the abandonment of unprofitable mileage. Over 73,000 miles, or 30 per cent of the total operated mileage carries less than 2 per cent of the traffic. The abandonment of this mileage, which surely must be very largely unprofitable, would save an enormous sum annually to the owning railroads. Taxes, generally speaking, are very high on terminal properties, especially where they are located in metropolitan districts. Where such terminals are largely occupied with the distribution of "less than carload" and in some instances high-class carload freight, the abandonment of the highly taxed metropolitan terminal and future distribution of goods in that area by motor trucks from terminals relocated outside of the metropolitan taxing area, suggests itself as a further opportunity to lower tax bills.

The Question of Railroad Wages

Average hourly wages of railway employes in 1931 were 157 per cent above the 1913 average, and in June, 1932, reflecting the 10 per cent deduction put into effect on February 1st and also some decrease in overtime, were still 131 per cent above 1913. Total monthly compensation per employe is not now so much above 1913 as is the hourly wage rate, due to the adoption of the 8-hour day upon the initiative of the employes. The hourly wage-rate comparison, however, is a true comparison of pay upon the basis of services rendered, and of the cost of wage increases to the railroads. It is true also that owing to the decline of railroad traffic drastic reductions have been made not only in the number of regular employes but in the number of days or hours worked each month. Average number of employes in July, 1932 was 1,022,000, which is the smallest number in any month for years back and contrasts with 1,309,793 in July, 1931 and an average of 1,660,850 for the year 1929. The brotherhood chiefs in their answer to the railroad officials say that not only have the railroad employes suffered a 40 per cent loss of employment but that a majority of those working had had only part time employment.

This is a deplorable situation, but it is obvious that the companies and employes are suffering together from lack of traffic, which is evidence that all of the industries of the country are suffering with them. The only remedy is more business throughout the country, more employment, more purchasing power among the people. The problem is to restore normal conditions in industry.

In their letter to President Hoover the brotherhood chiefs set forth their chief argument against another wage reduction as follows:

> We submit that our government cannot be indifferent to the menace of such a program, not only to the railway employes but to every one interested in promoting a revival of business. We submit that every effort to reduce wages, thereby further reducing purchasing power, will retard the forces of recovery.

This is in line with the arguments which the Federation of Labor has been offering throughout the last three years and without doubt represents the sincere opinion of both bodies of labor officials and of many other people. This view was generally accepted by the public, including the employing class, in the first year of the depression, but gradually the opinion has been spreading that it is a fallacious theory as applied to the present situation. There are occasions when wage increases are in order, not only as a matter of justice to particular groups of workers, but as a means of securing a better state of balance among the relationships of the industrial system. This is true if living costs are advancing faster than wages, which was the case at times between 1900 and 1914 and in the first two years of the war. It is not the situation at this time.

The Illusions of Money Wages

The effects of wage advances or reductions upon the total of purchasing power in circulation have been discussed in this number of the Letter (page 148) but certain points may well be emphasized. The essential point is that the argument so strenuously urged by the Labor officials exaggerates the importance of money wages in the economic system. It is based upon a misconception of the part which they play.

It is safe to say that nine-tenths of the controversies over such abstract wage questions as whether an increase of money wages increases the total purchasing power of the community are due to confusion over the function of money. The same is true of controversies over monetary systems. The idea that money in itself is original purchasing power, having had value put into it by a legislative decree, or that it comes from the bottomless pocket of an employer, befogs both subjects.

The War Rise of Wages and Prices

The great rise of wages and prices which occurred during the war, and to some extent in following years, and subsequent fall, affords an interesting study of the relations between wages and prices. The record gives a clear demonstration of the truth always held by economists that the general rise of the standard of living is achieved only by improvements in methods of production and distribution,

wage increases being only incidental thereto. Wages went up more than 100 per cent in a few years and since one man's wages make another man's cost of living, living costs went up also, but not quite so much, because the higher labor costs stimulated the use of labor-saving machinery and methods, and as reduced costs affected prices the cost of living declined. In 1920 wages were up 134 per cent from 1913 and the cost of living was up 116.5. The difference between these figures represents the real gain.

From that time on the studies of business managers to reduce their costs have been reducing living costs. By 1929, according to the Bureau of Labor, they were down to 71 per cent above 1913 and on June 15, 1932, according to the same authority, they were down to 35.7 per cent above 1913. Since 1929 the reduction has been largely at the expense of the farming population, for farm products are a leading factor in the cost of living, partly by the sacrifice of business profits, partly as a result of wage reductions and new economies of various kinds.

Even before 1929 complaints of the effects of "technological improvements" had been heard, for the changes of progress incidentally affect somebody unfavorably. The most impressive thing in the record is the fact that the standard of living is determined by the purchasing power of wages over commodities, not by nominal money wages.

Wages Always Comparative

All students of economics distinguish between "money wages" and "real wages," counting the latter as the true measure of compensation received. They recognize, broadly speaking, that the real compensation which a person receives for his own services in the economic system come to him in the products or services of others. There are economists in the service of the labor organizations who recognize this, and use it effectively when it suits their purposes to do so, which is whenever living costs are rising faster than wages. This was the case in early years of the war, and it was properly urged that unless wages kept pace with living costs the wage-earner was losing ground, even though his nominal pay was rising. Here is a quotation, very much to the point, taken several years ago from the "Labor Banker," a publication issued by the Brotherhood Investment Company, an organization affiliated with the Brotherhood of Locomotive Engineers:

The tendency upon the part of labor to estimate wages solely in terms of dollars frequently leads to serious economic error. The real significance of the wage labor received is not the dollar in hand but rather what the dollar will buy. Wages are always comparative. Cheap money means dear commodities; dear money means cheap commodities. The attention of labor is too frequently directed toward the dollar instead of the buying power of the dollar. Stabilization of prices is therefore one of the major economic issues so far as the working classes are concerned.

This virtually summarizes the argument offered above, "Wages are always comparative," and should be considered in their relations to commodities and the various services for which they are expended. So considered it cannot be said that any proposal has yet been made for a reduction of railroad wages to a level below that of the period preceding February 1, 1932. When the wage "deduction" was agreed to last February, the cost of living already had declined more than enough to reimburse the employes and is now much lower. Measured by purchasing power in the markets, railroad employes who have full employment have enjoyed an increase of compensation in a time of general distress.

Against this view the Brotherhood chiefs urge that unemployment and short time prevent their members from having the benefit of the existing wage rates. This is true but since it is a condition in which the whole country is involved it is not pertinent to a discussion of particular wage rates. When all classes are suffering from business stagnation it is impossible to compensate any particular group for its losses on that account. Any such compensation would come from people who are no better off than the complainants. A claim for such compensation is as good if made by the workers of all other industries against the railroad employes as if made by the latter against the former; perhaps better, for the influence of transportation costs is more widespread than the influence of costs in most of the industries. But when everybody has a claim of that kind against everybody else, all might as well be dropped. We repeat that the only remedy is by getting all industry back to normal conditions. Furthermore, there is reason to believe that the rigidity of certain high wage rates which were fixed under conditions that were very different from those existing today is largely responsible for the present situation.

(On account of lack of space in this number the remainder of this article is carried over to the November issue of the Letter.)